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In The
Supreme Court of the United States
October Term, 1988

UNITED GAS PIPE LINE COMPANY,

Petitioner,

vs.

LOUISIANA POWER & LIGHT COMPANY,

Respondent.

On Petition For Writ Of Certiorari To The
Louisiana Court of Appeal, Fourth Circuit

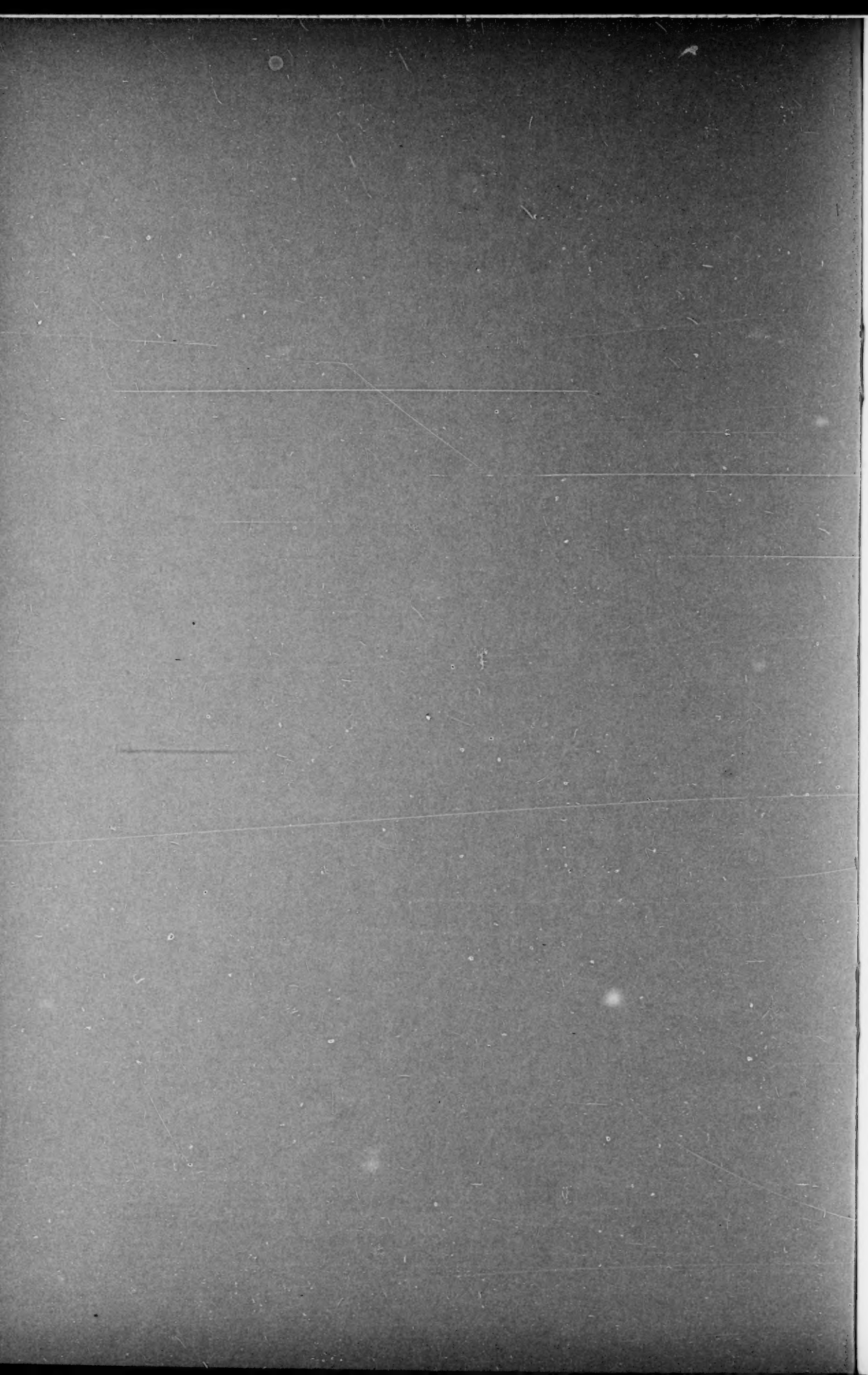
**BRIEF FOR LOUISIANA PUBLIC SERVICE
COMMISSION IN OPPOSITION TO THE PETITION**

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QUESTION PRESENTED

When the courts of a State determine that a pipeline's failure to perform its contractual obligations was caused by its own failure of due diligence, unreasonable conduct, imprudence, improvidence and inadequate planning, should this Court overrule a liability judgment against the pipeline under a preemptive federal liability standard of "negligence," simply because the word "negligence" was not used by the State courts in describing the conduct of the pipeline?

STATEMENT REQUIRED BY RULE 28.1

The Louisiana Public Service Commission ("Louisiana Commission") is an agency created by the Louisiana Constitution. La. Constitution Article IV § 21. The Louisiana Commission is not incorporated and accordingly has no parents, subsidiaries or affiliates other than the State of Louisiana.

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STATEMENT OF THE CASE

1. United Gas Pipe Line Co. ("United") seeks a writ of certiorari to review decisions of the Louisiana State courts holding United liable for breaching gas supply contracts with Louisiana Power & Light Co. ("LP&L"). United does not dispute the courts' finding that it failed to perform the contracts. United asserts that the judgment conflicts with a preemptive federal liability standard of "negligence" that is applicable to its contract curtailments. This negligence standard was finally articulated by the United States Court of Appeals for the Fifth Circuit after the issuance of the written opinions of the Louisiana courts in the contract litigation. Although the Louisiana courts found that United failed to exercise due diligence, engaged in inadequate planning, was unreasonable, improvident and imprudent, and that its own fault caused the curtailments, United argues that the State court decision is invalid because it assertedly does not conform precisely to the language employed by the Fifth Circuit. (App. 9c, 15a, 21a, 86a, 89a, 94a, 97a; Pet. at 21-26).

Beginning in 1971, United failed to deliver to LP&L the quantities of gas required under their long term gas supply contracts. The delivery shortfalls resulted in increased costs to LP&L for substitute fuel, conversion of generating facilities to use other fuels, and increased operation and maintenance expense. The increased costs were ultimately borne by the customers of LP&L through increased rates.

The failure of United to perform its contracts resulted in parallel State and federal litigation. In 1974, LP&L filed a contract damage suit against United in the Civil District Court for the Parish of Orleans ("district

court").¹ That suit led to the judgment that United asks the Court to review, which was issued in 1984 and affirmed on appeal by the Louisiana Court of Appeals for the Fourth Circuit ("State court of appeal") in May, 1987 (App. 77a-113a; 1a-75a). In addition, United filed curtailment proceedings before the Federal Power Commission ("FPC"). These proceedings led to the adoption by the Federal Energy Regulatory Commission ("FERC") in 1985 of a tariff provision limiting the circumstances in which United could be deemed liable for contract damages. (App. 115a-140a). The decision was affirmed and explained by the Fifth Circuit in August, 1987. (App. 141a-203a). The liability standards advocated by United in both the federal and state courts, which would have exonerated the pipeline in the absence of bad faith or willful misconduct, were rejected. (See App. 176a, 177a-185a; 17a-18a).

2. The contract liability trial commenced in the district court in January, 1982. The trial consumed two and one-half years. After the submission of the case, the district court issued an opinion finding that United breached its contract obligations through its own failure of due diligence. The district court specifically found that United was "imprudent." (App. 89a). This finding satisfied the "prudence" standard then advocated *by United* in the FERC proceeding as the basis for contract liability. (App. 123a-124a). The district court also determined that the "improvident actions" of United caused its gas shortage, the shortage could have been avoided by "the exercise of

¹ The Louisiana Public Service Commission ("Louisiana Commission") which authorized the pass through to customers of the increased costs resulting from the failure of United to perform the contracts, intervened in the district court on the side of LP&L to assist in the recovery of those damages for the benefit of LP&L's customers.

due diligence," the shortage was caused by "imprudent management decisions," and United "failed to take adequate steps to determine the implications of its actions or to assure an adequate supply to meet the obligations of the company." (App. 86a, 89a, 97a, 89a). The district court did not assign the burden of proof on the "fault" issue to United, but affirmatively determined that United was at fault based on the evidence.

In a lengthy opinion, the State court of appeal upheld the decision of the district court. It affirmed the finding that "United did not exercise the reasonable foresight that good faith performance of its contracts required." (App. 15a). Further, it determined that the actions of United "did not constitute a reasonable effort to perform [the firm requirements] contracts" and did "not constitute good faith performance of its obligations." (App. 9a, 15a). In addition, in holding that the federal fault standard was satisfied, it referred to and relied on the district court's finding that the gas shortage " 'was induced by the unrealized expectations and imprudent decisions of United and its management.' " (App. 17a, 17a-18a). The State court of appeal acknowledged that the State could not impose liability "akin to strict liability or liability without fault," but determined that it could impose liability for breaches "by negligence or lack of due diligence." (App. 18a). This articulation of the appropriate standard is very similar to that ultimately articulated by the Fifth Circuit; it was adopted instead of the "willful misconduct or reckless disregard" standard then advocated by United. (App. 17a-18a).

After the decision of the Fifth Circuit, the State court of appeal denied rehearing and the Louisiana Supreme Court denied an application for review filed by

United. (App. 76a, 114a). These decisions implicitly rejected the arguments raised by United in this Court. In separate orders, the Louisiana Supreme Court denied review of rulings of the State court of appeal dismissing claims of LP&L against United and Pennzoil Co. based on alleged antitrust violations and tortious interference with contract. *Louisiana Power & Light Co. v. United Gas Pipe Line Co.*, No. 88-C-0619 (La. 1988); *Louisiana Power & Light Co. v. United Gas Pipe Line Co.*, No. 88-C-0409 (La. 1988). LP&L did not seek review of the State court decisions rejecting its claims for about \$138 million for loss of generating capability and \$10 million for conversion costs and certain expenses. (App. 108a, 59a, 63a, 66a-67a).

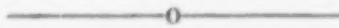
3. Before the FERC and the Fifth Circuit, United advocated a uniform federal fault standard for contract liability. At the FERC, United asserted that "prudent management" should be the standard. (App. 123a). It also argued that it should be exonerated from liability by the FERC. (App. 124a). In the Fifth Circuit, United argued that it should not be held liable absent bad faith or willful misconduct. (App. 176a).

The FERC rejected United's exoneration arguments and held that the federal interest required only that United's tariffs exculpate United from contract liability for curtailments if United did not cause the shortage of gas through its own "negligence, bad faith, fault or willful misconduct." (App. 131a-132a).

The Fifth Circuit rejected both absolute exculpation and the bad faith/willful misconduct standard proposed by United. In doing so, the court analyzed the reasons for adopting the fault standard and then determined the standard needed to accomplish those goals. The Fifth Circuit reasoned that:

- a) A pipeline that curtails in accordance with the federally-approved plan cannot be held liable in damages if those damages were caused “*solely* by its compliance with the federal curtailment scheme” because it “would create incentives for the pipelines to resist a federal curtailment scheme.” (App. 178a-179a) (emphasis added).
- b) However, “. . . it is *not* in the public interest to immunize a pipeline from liability for its own negligence or willful misconduct.” (App. 179a).
- c) If mere compliance with a curtailment plan were to shield a pipeline from all liability “a pipeline could contract to deliver more gas than it knows it is able, relying on the federal curtailment scheme to immunize it. Thus, incentive for prudent management would be undermined.” (*Id.*)

As the court stated, “liability flows . . . from United’s mismanagement in causing the shortage of gas, creating incentives for United to manage properly its gas supply and demand.” (App. 180a). Therefore, if United’s mismanagement caused the shortage that necessitated curtailments, the “federal standard” affords United no exculpation. (App. 180a). Indeed, the imposition of liability would be in the “federal interest.” (*Id.*)



REASONS FOR DENYING THE WRIT

Summary of Argument

1. The petition of United does not present an issue worthy of this Court’s review. Contrary to United’s assertion, the State court judgments attack neither the authority of the FERC nor the federal standard of liability it established. The Louisiana courts acknowledged the federal interests and applied the federal standard. The record fully supports the imposition of liability for the fault of United in breaching its contracts.

2. United incorrectly attempts to portray this case as a conflict between federal and state authorities. United is forced to emphasize semantics, because there is no substantive difference between the federal and State fault standards. The Louisiana courts found that United itself caused the shortage on its own system through a history of improper and imprudent management of its gas supply. The findings of the State courts are more than sufficient to satisfy the Fifth Circuit's "negligence" standard. In addition, they are consistent with findings made by a federal district court. These findings are not properly subject to review in this Court. *See Lloyd A. Frey Roofing Co. v. Wood*, 344 U.S. 157, 160, 73 S.Ct. 204, 97 L.Ed. 168 (1952).

3. The record provides overwhelming support for the imposition of liability under the standard articulated by the Fifth Circuit. United mismanaged its reserves and supply obligations, knowingly failed to take reasonable steps to ensure an adequate supply, misled its regulators, and diverted assets to its parent that would have been used to acquire gas supplies. Even if the fault standard articulated by the State courts were substantively different than that adopted by the Fifth Circuit, reversal of their decision would not make any difference, because the record and the factual conclusions of the State courts establish that United's misconduct far surpassed the minimal federal requirement for imposing liability. Reconsideration of the case would not lead to a different result.

4. The FPC Order allocating the gas supplies of United provides no defense to contract liability. The allocation of gas supplies was the natural result of the gas shortage caused by United's fault. Since United caused the shortage, and curtailments were the foreseeable consequence of the shortage, United is responsible for failing to

fulfill its commitments. This conclusion fully comports with the Fifth Circuit decision. Therefore, the writ should be denied.

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ARGUMENT

I. **The Standard Employed by the State Courts Does Not Conflict With the Federal Standard of Liability or Any Federal Interest.**

United contends that the State court judgments present a “collateral attack” against the rulings of the FERC and the Fifth Circuit and “undermine” the federal interest in the regulation of interstate pipelines. (Pet. at 13 *et seq.*, 17). The State court findings, however, fully support the imposition of liability under the federal standard. United does not refer to the evidence to support its argument, but points to variations in the terminology used by the Louisiana and federal courts. These semantic variations result not from substantive differences, but from the fact that the State court decisions are independent of and predate the Fifth Circuit decision.

The Fifth Circuit affirmed the determination by the FERC that the

federal interest require[s] the abrogation of contract liability based *solely* on compliance with a filed curtailment plan, but [does] not require exculpation when a pipeline causes the shortage by negligence or wrongful misconduct. (App. 178a) (emphasis added).

As United notes, the Fifth Circuit indicated that the party claiming damages must prove that the negligence of United caused the shortage. This standard is satisfied here. The plaintiffs undertook to prove, and did prove, the fault of United in causing the shortage. The Louisiana courts specifically found that United’s mismanagement and negligence caused its shortages. Thus, the imposition of lia-

bility furthers, rather than undermines, the federal interest.

Although predating FERC Opinion 237 and the Fifth Circuit opinion, the district court decision recognized that a liability judgment must comply with a federal fault standard. It stated:

Although curtailment tariffs and FPC/FERC curtailment orders would ordinarily exculpate a pipeline from contractual liability for curtailments, such tariffs and orders . . . will not exculpate United . . . because the Court is of the opinion that United's shortage of supply was induced by the unrealized expectations and imprudent decisions of United and its management. (App. 94a).

The trial court rejected United's contention that liability was being imposed solely because of United's compliance with curtailment orders. It found that United's curtailments, and the damages occasioned thereby, were caused by United's fault and lack of due diligence.

The district court did not assign the burden of proof on the fault issue to United. Based on the plaintiffs' affirmative proof, it made specific findings that United's own failure of due diligence and mismanagement, and *not* forces beyond its control, were the cause of the shortages and the ensuing damages. The district court found: 1) that the gas shortage was "caused by United's improvident actions," 2) United improperly released large quantities of reserves, 3) United failed to attach adequate new reserves to its system, and 4) United increased its sales without attaching adequate reserves to meet foreseeable customer requirements. (App. 86a, 90a). Moreover, the district court determined that United "improvidently" released reserves on its New Orleans District Five intrastate system, failed to attach available gas reserves, and

should have foreseen the ensuing shortage. (App. 86a). Further, the district court determined that United failed to exercise "due diligence" in managing its gas supply. (App. 89a). In addition, the district court found that United was "imprudent." It said:

United's management was imprudent in permitting its gas supplies to dwindle, relative to its delivery obligations, to an amount that did not permit adequate service to customers. The management failed to take adequate steps to determine the implications of its actions or to assure an adequate supply to meet the obligations of the company. (App. 89a).

The district court left absolutely no doubt that the fault of United was the cause of the gas shortage and the ensuing curtailments. It stated:

The Court is of the opinion that the shortage is the cause of the damages. . . . United's imprudent management decisions caused its shortage. United's failure to deliver the contract volumes . . . is due to a *shortage of gas on its systems which United could have avoided by the exercise of due diligence*. (App. 97a) (emphasis added).

Further, the district court found that "United's improvident actions" were the reason for governmental orders prorating gas. (App. 90a).

The decision of the district court fully conforms with the Fifth Circuit's fault standard. As the Fifth Circuit noted, "negligence is generally defined as the failure to exercise reasonable care, that is, the degree of care which a person of ordinary prudence would exercise in the same or similar circumstances." (App. 182). The district court found that United did *not* exercise the care a prudent person would have exercised in the circumstances and took unreasonable, improvident actions despite foreseeable harm to its customers. Moreover, the district court determined

that United's fault caused the gas shortage and ensuing curtailment orders. These findings were based on the affirmative proof of the plaintiffs, who undertook to prove fault in light of the pending FERC proceeding.

The decision of the State court of appeal is also consistent with the "federal standard" that United now argues must be applied. On appeal, United urged the Louisiana Court of Appeal to reject FERC Opinion 237 as an incorrect statement of the federal standard for liability. United argued for a uniform standard of exculpation absent willful misconduct or recklessness. (App. 17a-18a). Notwithstanding United's misdirection, the State court of appeal acknowledged the existence and limitations of the standard established by the FERC and approved four months later by the Fifth Circuit. The court properly started from the premise that federal tariffs may "override state law liability akin to strict liability or liability without fault," but "*breaches of contract not only by willful misconduct, but also by negligence or lack of due diligence, are governed by state law standards.*" (App. 18a). (Emphasis added). The State court of appeal considered the record and affirmed the district court's findings of fault.

The court first analyzed United's actions affecting its New Orleans District Five intrastate system. It noted that between 1962 and 1969 United released almost 2.1 trillion cubic feet of gas attached to the intrastate system and shifted another 269 billion cubic feet to its interstate system. Those released reserves would have provided sufficient gas to cover the intrastate system's needs for over thirteen years. (App. 9a). The court rejected United's contention that its management of its gas supplies was reasonable in the circumstances. (App. 11a).

The State court of appeal specifically found that the asserted added cost of performance did not justify non-performance by an entity the size of United. (App. 11a). The court compared the added costs to the size of United's sales and determined that the cost could not reasonably justify nonperformance. As noted by United, the State court of appeal determined that the requirement of contractual performance typically is not dependent on cost. United fails to report, however, that the court went further and analyzed the cost issue, concluding that the costs were "not so excessive . . . as to justify nonperformance". (App. 11a).

The court also analyzed United's gas sales and acquisition activities for its interstate system, which served LP&L's Sterlington generating facility. (App. 10a-11a). It determined that United's reserve management practices on its interstate system were also unreasonable. While sales were increasing, the company released reserves and failed to acquire quantities of gas sufficient to even match the reserves it released much less its sales. The State court of appeal concluded:

The record shows that there was no gas shortage in the early 1960's, and the trial judge's conclusion was therefore reasonable that United could have acquired additional reserves that, coupled with the reserves it released, would have maintained its reserve position and its ability to fulfill its contractual obligations over the lives of the contracts at issue. (App. 11a).

The State court of appeal specifically rejected United's argument that the federal curtailment orders exonerate United from liability, but it did so not because it rejected the federal authority, but because it found that the curtailment orders would not have been necessary ex-

cept for the fact that "United did not exercise reasonable foresight". (App. 15a, 4a).

The State court of appeal did state in its opinion that United had the burden "to prove its defenses." (App. 15a). This statement reflects the fact that the court was required to deal not only with the interplay of federal and state liability standards, but with a bevy of affirmative contract defenses raised by United. (App. 18a-20a, 12a-17a). Nevertheless, the court recognized that federal interests prevented the imposition of liability absent "negligence or lack of due diligence," or greater fault. (App. 18a). It affirmed the district court's affirmative conclusion "that United did not exercise the reasonable foresight that good faith performance of its contracts required" and reviewed some of the proof supporting this determination. (App. 15a, 9a-11a). The affirmative determinations of the State court of appeal more than satisfy the federal standard, especially since the court affirmed the more comprehensive findings of the district court.

United belittles the findings of the State courts, but its conduct has led to similar conclusions in federal settings. The federal district court for the District of Columbia is the only other court that analyzed United's actions relating to the shortages on its systems. That court also concluded that United was at fault in causing the shortages that led to curtailments, and this fault violated a federal fault standard of due diligence. The opinion was withdrawn after a settlement. *Texasgulf, Inc. v. United Gas Pipe Line Company*, 610 F. Supp. 1329 (D.C. D.C. 1985), *opinion withdrawn*, 617 F. Supp. 41 (D.C. D.C. 1985). The FERC denied United's request that the FERC issue findings of fact that United had not violated the federal standard of care, because the issue was beyond the

scope of the Phase III curtailment proceedings. The FERC did note, however, that the administrative law judge had suggested that improper management decisions by United were causally related to the curtailments. (App. 124a, n. 12).

Both of the Louisiana courts applied the appropriate standard in analyzing United's actions. United was found liable not simply because it failed to deliver the contract quantities of gas, but because its own negligence, fault and mismanagement caused the shortages on its systems. The federal interest is served by permitting the decisions of the Louisiana courts to stand. The semantic arguments of United provide no basis for overturning the product of years of litigation. Therefore, the writ should be denied.

II. The Finding of Liability is Supported by Overwhelming Evidence Satisfying the Federal Standard, So That Reconsideration of the Case Could Not Change the Result.

The semantic arguments of United reflect no substantive difference in the standard articulated by the Fifth Circuit and applied by the State courts. If anything, the affirmative findings of the State courts go far beyond the threshold of fault required before imposing liability under the federal standard. In addition, the evidence supports the conclusion that United's misconduct was more than negligent. Reversal of the decision—and reconsideration by the State courts—simply could not change the result based on this record.

Beginning in 1960, United embarked on three inconsistent courses of action that virtually guaranteed its inability to fulfill its contract obligations by the early 1970s. First, United aggressively increased its sales of gas. At the same time, United voluntarily released huge volumes

of dedicated reserves. Although sales were promoted and reserves released, United did not aggressively acquire new reserves to meet its increasing contract obligations.

From 1960 to 1968, United never bought as much gas as it sold or lost in any year. (Tr. at 5123; NOPSI Ex. 21). United's reserves were depleted by over 17 trillion cubic feet of gas, but only four trillion cubic feet were acquired.² This depletion of the system occurred in the context of facts showing that United mismanaged its system, knew the consequences of its actions, misled its regulators, manipulated the federal-state regulatory scheme, and depleted its own assets to pay inordinate dividends to its parent. These actions would satisfy virtually any liability standard.

First, United mismanaged its gas system. Gas supply and sales decisions were made and implemented without any concern for their impact. That lack of planning created the shortage and prevented United from responding effectively to the situation.

United did not have a management mechanism to match supply and demand. Indeed, its managers from relevant departments denied responsibility for ensuring that supplies were adequate. Huge volumes of reserves were released without any analysis of the consequences of this action.

² NOPSI Ex. 21. Of the 2.8 trillion cubic feet acquired in 1966-1968, approximately 1.8 trillion cubic feet or 63% of all additions, were acquired for United's Texas intrastate system and thus were unavailable to serve either the interstate system or the New Orleans District 5 intrastate system in Louisiana. (The Texas intrastate system was transferred to Pennzoil Pipe Line Co. on January 1, 1970, less than a year before curtailments began.)

Mr. Glen Sanders, the head of United's economic planning section from 1964 into the 1970s, testified that although his department prepared five-year peak day studies, that department "never did have the responsibility for determining the adequacy of the reserves." (Tr. 5794-95). Rather, he stated, it was "top management" which had the responsibility to insure an adequate supply of gas. (Tr. at 5795).

Mr. Ed Parks, the president of the company from 1956 to 1967, as a member of "top management", should have been one of those responsible for assuring that supplies were adequate. Mr. Parks testified to the following: United "had no specific goal for the ideal amount of reserves that should be held by the company;" it had no policy regarding an appropriate reserve-to-production ratio from 1960 to 1965; he never saw any "studies of the effect of the release of reserves on the ability of the company to service customers;" and he knew of no studies performed by United in the early to mid 1960s to project the availability of future gas supplies. (Tr. at 5985; 6991; 6985; 6980).

The reserve section of the company was responsible for estimating gas supplies. Mr. Byron B. Gibbs was a member of that section from 1947 to 1965 and that section reported to him from 1967 to 1976 (Tr. at 7663-64, 7788). Mr. Gibbs testified that he was aware of the steady decline of reserves of United throughout the 1960s, but he didn't consider it necessary to bring the declining reserve situation to the attention of top management because he thought they were "on top" of the situation. (Tr. at 7785).

In 1967, a report prepared by the Arthur D. Little, Inc. consulting firm concluded that United released re-

serves "without much thought for the future." (GSU Ex. 127). The district court also concluded that United released reserves without analyzing the impact of this action. It stated:

At the time that United entered into its contracts with NOPSI, LP&L, and its other customers, United knew that it did not have enough gas under contract to meet its delivery obligations for the life of those contracts. United was aware of an increase in competition for new reserves. By promising to sell gas that it did not own, United knew or should have known that there was a risk that it would not be able to get gas at favorable prices to meet increasing demands or obligations. *However, United managed its system on the assumption that it could always get additional gas in the future whenever needed, wherever needed and at an advantageous price to meet the obligations already committed.* (App. 89a-90a) (Emphasis added).

In sum, United acted with no regard for the consequences of its acts.

Second, the impending gas shortages were not only foreseeable but actually were made known to United long before curtailment began. In 1966, United engaged the consulting firm of Stone & Webster Service Corporation to prepare a report for United's management on the operations of the pipeline company. That report, delivered in January, 1967, specifically addressed the adequacy of United's reserves to meet its sales obligations. Stone & Webster warned United that a shortage of gas on its system was imminent. The report stated: "The present reserves will be able to meet annual sales requirements through 1968 when local shortages will begin to appear, first in the Houston intrastate system." (LPSC Ex. 41 at 62). Stone & Webster recommended that United base

its long range acquisition and sales plans on the assumption that there would be a basic shortage of natural gas. The report stated:

Probably the most important determinant of United's long-range future is the basic question of whether United and the gas industry are faced with a shortage or surplus of new supplies relative to requirements. *We believe that the most probable condition and the one on which United should predicate its long-range planning is that of a basic shortage.* (*Id.* at 64). (Emphasis added).

The report further stated that United must acquire a total of 25 trillion cubic feet of additional reserves by 1976 in order to have a fourteen year remaining life index at that time. (*Id.*) Yet, United acquired barely two trillion cubic feet of gas in the next four years for its interstate system. (NPSI Ex. 21; LPSC Ex. 42).

Stone & Webster was not the only independent consultant to advise United of the impending shortages. Also in 1967, Pennzoil United, Inc., United's parent, commissioned the Arthur Little firm to study United's operations. The Arthur Little report concluded that the acquisition of additional reserves was the most important factor affecting United's future and recommended an aggressive acquisition program. The report found that United's reserve position was substantially below both the national reserve-to-production ratio and the average reserve coverage of all interstate pipelines. (GSU Ex. 129, p. 2). It also concluded that the company's deliverability life was short. Arthur Little recommended that United adopt a slower rate of growth in sales—3%—which still would require a program of aggressive reserve acquisition of one trillion cubic feet of new reserves each year. (*Id.*, p. 3).

United's own economic and planning division in 1966 urged the company to acquire additional reserves. It warned that "United needs additional reserves to maintain its existing sales level of over 1.3 trillion cubic feet per year." (GSU Ex. 117, p. 8). Further, United's own five year and ten year studies conducted throughout the 1960s forecasted that the reserves then connected to United's systems would be inadequate to meet its customers' requirements. (Tr. 4975-76).

Third, United failed to take reasonable steps to prevent a shortage, even after it was informed by consultants of the impending danger. From 1967 until the commencement of curtailments United took the following steps:

- (a) United increased its sales from 1.2 trillion cubic feet a year in 1967 to 1.5 trillion cubic feet a year in 1970, a sales increase of 25 per cent. (NOPSI Ex. 21, LPSC Ex. 42).
- (b) Excluding sales and additions to the Texas intrastate system, United's sales and reduction in reserves due to contract terminations exceeded gas acquisitions by over 4.4 trillion cubic feet from 1967 to 1970. (*Id.*)
- (c) United continued to make sales to new customers including Mississippi River Transmission Corp., Escambia Chemical Corp., and others (GSU Ex. 151, 152).
- (d) United acquired a majority of its reserves for the Texas intrastate system, which could not be used to serve the interstate system or the New Orleans District Five intrastate system. (NOPSI Ex. 21, LPSC Ex. 42). More reserves were attached to the Texas system than to the interstate or District Five systems, although annual sales from the interstate and District Five systems exceeded those of the Texas system by almost six times.

(NOPSI Ex. 21, pp. 2, 3 (adjusting for Sea Robin); Tr. 6065-69).

Fourth, United repeatedly submitted inaccurate information to federal regulators suggesting that the company had more gas reserves than were actually attached to its systems. This practice confirms that United knew or should have known that it would be unable to meet its contractual undertakings.

Beginning in 1964, United was required to file annually a Form 15 with the FPC. The Form 15 was designed to provide the FPC with detailed information on gas reserves attached to pipelines subject to its jurisdiction. This information was essential to the FPC since it had to approve pipeline applications to add new or enlarged service to their interstate systems. However, United supplied the FPC with inaccurate and misleading information.

Despite United's release of huge quantities of reserves in the 1960s, its Form 15 reports to the FPC continued to reflect those released quantities as reserves attached to its system. The *Texasgulf* court described United's actions as follows:

United's Paradise field was released to the producer, Texaco, in 1963. United's Lirette field was likewise released to the producer, Humble, in 1964. However, United's Form 15 reports for 1963, 1964 and 1965 continued to report these fields as attached to United's system. Both were major fields with reserves totaling 1,205 Bcf, and the inaccurate reporting had the effect of exaggerating United's dedicated reserves by five percent in 1964 and six percent in 1965.

610 F.Supp. at 1348.

In addition, the company's 1969 Form 15 included as dedicated gas reserves over 2.3 trillion cubic feet of gas from the "Sea Robin" project, although those reserves were not yet proven. (Tr. 7775-77).

United's misreporting of reserves to the FPC was not confined to instances of unproven or already released quantities of gas. Although the Form 15 was designed to permit the FPC to evaluate whether it should be permitted to make additional sales of gas from its *interstate* system, United included *both its inter and intra state* reserves in its reports, thereby falsely exaggerating its available reserves. A consultant employed by United described the inclusion of intrastate reserves on its Form 15 as follows:

If the intrastate gas supply were omitted from the 1967 Form 15, it would give the appearance of a cut in UGPL's reserves of approximately six trillion cubic feet. This large apparent cut in reserves plus the fact the merger proceeding has not been completed could cause UGPL quite a bit of trouble in pending FPC proceedings. (NOPSI Ex. 33).

The "merger proceeding" referred to was the merger between United and Pennzoil.

Not only did United's Form 15 filings overestimate reserves, they also *underestimated* the company's sales requirements. Mr. Sanders testified that between 1961 and 1970 United's sales grew at an annual compound rate of 3.3%. (Tr. 5904-07). The projected sales reported to the FPC, however, were quite different. These projections were the basis for determining the potential life of United's reserves. In its 1963 Form 15 United projected that from 1966 to 1983 there would be *no* growth in sales. (Tr. 5914-15). Mr. Sanders admitted, however, that notwith-

standing this report, United in fact did not believe that its sales would be level for eighteen years. (Tr. 5226). United's 1968 Form 15 projected that over the next twenty years United's sales would *decline* on average. (Tr. 5917-19). At the same time United was submitting these decreasing sales projections to the FPC it was applying for certification to serve new customers. (Tr. 5919).

United was thus experiencing sustained growth in sales throughout the 1960s, but reporting that sales would decrease in the future. United had released huge quantities of dedicated reserves and failed to acquire reserves to even meet its then-present needs. All this time, United was aggressively seeking new customers. The reason behind its misreporting is obvious—unless United could show that its reserves were sufficient, the FPC would fail to certificate new sales. This misreporting of reserve and sales figures to the FPC establishes that United knew or should have known that it would be unable to meet its contractual requirements in the future.

Fifth, during the 1960s, United and its parent, Pennzoil, manipulated both the flows of gas and the supplies dedicated to United's various systems. Their activities indicate a knowledge that shortages would occur on those systems.

In the 1960s United operated at least three distinct pipeline systems: the New Orleans District Five intrastate system; a Texas intrastate system; and its interstate system. Only the interstate system was subject to FPC jurisdiction. It was unlawful for United to use interstate gas in its intrastate systems without prior FPC approval. 15 U.S.C. § 717f(c). Notwithstanding that prohibition,

in 1965, United began injecting interstate gas into its District Five intrastate system without obtaining an FPC certificate authorizing this action. No notice of these injections was given to the FPC or to the Louisiana Commission, which had regulatory jurisdiction over the New Orleans District Five system. Those injections of interstate gas into the intrastate system continued and expanded through October, 1970. (App. 84a-85a).

United was fully aware that FPC approval was required for the action it undertook. (GSU Ex. 132, Tr. 14815, 14870, 13585-86, 13754-56). Applications to the FPC for authorization to convert the intrastate system to an interstate system were prepared by United in early 1967 but were not submitted for over three years. (LP&L Ex. 28). While United continued to inject interstate gas into the intrastate system, it released significant reserves attached to the New Orleans District Five system and failed to acquire sufficient reserves to meet the needs of its Louisiana intrastate customers. The trial court found that United's mismanagement of its supply and demand coupled with the injections of interstate gas created a shortage on the intrastate system that "could have and should have been foreseen by United." (App. 86a).

United's failure to notify the FPC of the interstate gas injections into its District Five System was intentional. While its reserves on its interstate and District Five systems dwindled, United was acquiring *some* reserves. However, the vast majority of reserves acquired after the unauthorized flows began were attached to the Texas intrastate system that was transferred to another Pennzoil subsidiary in 1970.

United thus bought time to strengthen its Texas intrastate system, which was spun off. At the same time, United depleted reserves on its interstate and District Five systems, making shortages and the ensuing curtailments inevitable.³ United filed its application to operate District Five as an interstate pipeline on October 1, 1970. Twenty-six days later it filed a petition with the FPC seeking to curtail deliveries of gas to its interstate customers, including District Five, alleging that there was a shortage of gas on its interstate system. (NOPSI Ex. 228). The Texas intrastate system retained its intrastate status and was not subject to FPC curtailment jurisdiction.

Sixth, beginning in 1966, Pennzoil, United's parent, systematically siphoned available cash from United, leaving the company without the resources needed to acquire additional reserves. Pennzoil effectively took control of United in 1966, five years before curtailments began. Between 1966 and 1970 United had total earnings of \$80 million, but paid out \$109 million in dividends to Pennzoil. (LPSC Ex. 50, at 1, 6; Tr. 20,640) In 1968 alone, after the issuance of the Arthur Little and Stone & Webster reports urging United to drastically increase its reserve acquisitions, United paid Pennzoil \$67 million in dividends, although United's entire earnings for that year were only \$16 million. (LPSC Ex. 50, at 1).

This consistent pattern of paying more in dividends than United earned, despite a critical need to acquire re-

³ After the Texas intrastate system was spun off, the remainder of United had a reserve-to-withdrawal ratio of 9.46 while the former Texas intrastate system had a reserve to withdrawal ratio of 23.57. (Tr. 6088 see also NOPSI Ex. 21, pp. 2, 3, Tr. 6065-69).

serves, does not reflect prudent management. United allocated corporate resources in a manner fundamentally inconsistent with its regulatory and contractual obligations. It sacrificed the needs of customers to satisfy the desire of its parent.

These factors buttress the conclusion that United was at fault. In addition, although United contends that the Louisiana courts failed to consider United's actions vis-a-vis those of other major pipeline companies, those analyses were performed. (Pet. at 22). They reveal that United fell woefully short of industry standards in reacting to the shortages.

James T. Mitchell, an expert witness who testified on behalf of Gulf States Utilities, Inc., analyzed United's performance against the performance of thirteen comparable pipelines. (GSU Exhs. 173-180). The analysis revealed that the reserves of the comparable pipelines increased at a steady rate in the 1960s while United's reserves decreased dramatically (Tr. 7991, 8001-04). In addition, United curtailed more than any of the comparable pipelines from 1972 through 1977. (GSU Ex. 179). Furthermore, in 1979-1980, when many of the other pipelines had ceased curtailment, United was still curtailing over 40% of its firm delivery requirements. (*Id.*).

A comparison of United's performance against intrastate pipelines operating within Louisiana is also instructive. Numerous intrastate pipelines operated in Louisiana in the 1960s and the 1970s. Other than United, these included Texaco, Louisiana Intrastate Gas System, Sugar-bowl, Monterey, Continental Oil Company, Creole, and Shell. (Tr. 25073-25075). Only United curtailed deliver-

ies prior to 1978. Texaco began minor curtailments in 1978, while the others had no curtailments. (*Id.*). Therefore, when compared to other intrastate pipelines, the inescapable conclusion is that United could have avoided the shortages on its intrastate system.

III. The Federal Standard Does Not Support Exculpation Of United Because of the FPC Order Eliminating the Power Plant Preference.

United argues that the Louisiana courts erred because they rejected United's contention that it should be exculpated for delivery shortfalls that followed FPC Opinion 647, which eliminated the power plant preference. (Pet. at 24). Opinion 647 changed the ranking of United's customers in the curtailment scheme so that its direct sale customers were placed in a low priority. F.P.C. Opinion No. 647, *United Gas Pipe Line Co.*, 49 F.P.C. 179 (1973). United's arguments ignore a fundamental premise of the Fifth Circuit decision. The Fifth Circuit Court ruled that United should not be exonerated from liability by compliance with a curtailment scheme, where its own fault caused a *shortage* that resulted in curtailments. The court stated:

[I]f compliance with a filed curtailment scheme in all cases protects a pipeline from liability, a pipeline could contract to deliver more gas than it knows it is able, relying on the federal curtailment scheme to immunize it. Thus, incentive for prudent management would be undermined. (App. 179a).

This court found that liability flows "from United's mismanagement in causing the shortage of gas. . . ." (App. 180a). If the pipeline causes the shortage, and curtailments are foreseeable, the pipeline should be held liable for its failure to deliver contract quantities. (App. 183a).

Since all curtailment schemes establish delivery priorities, it is the foreseeability of the *need to curtail* which establishes liability, not the foreseeability of specific curtailment allocations.

The findings of the state courts comport with the federal standard. As the district court stated:

The Court is of the opinion that the shortage is the cause of the damages, not the action of the FPC in trying to deal with the results of United's shortage. The curtailment orders did not cause the shortage, United's imprudent management decisions caused its shortage. United's failure to deliver the contract volumes is not attributable to the FPC's curtailment plans proposed and supported by United. Its failure is due to a shortage of gas on its systems which United could have avoided by the exercise of due diligence. (App. 97a).

The federal district court in *Texasgulf* reached a similar conclusion. *Texasgulf, Inc. v. United Gas Pipe Line Co.*, 610 F.Supp. 1329, 1339 (D.C. D.C. 1985), *opinion withdrawn after settlement*, 617 F.Supp. 41 (D.C. D.C. 1985). (A prerequisite for exculpation "is the existence of a gas shortage not caused by United's lack of due diligence.")

The Louisiana courts determined that United failed in its obligation to prudently manage its gas supplies. Curtailments were the foreseeable result of United's mismanagement. Accordingly, United should bear the expense of compensating for that mismanagement.

CONCLUSION

This case presents no issue worthy of the Court's consideration. The federal standard of liability has already been established and the decision of the Fifth Circuit is final. This case was decided on facts not likely to be re-encountered, as United has settled most of the lawsuits arising from its curtailments. The findings of the state courts comport fully with the federal liability standard adopted by the Fifth Circuit, and the record would support liability under a more stringent standard. Given the findings already made by the courts and the evidence, a remand for consideration of the semantic variations advocated by United could not conceivably alter the result. Therefore, the writ should be denied.

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